

# **BUSINESS LAW SECTION**

## **CORPORATIONS COMMITTEE**

### **COMMITTEE MEETING MINUTES FOR JULY 12, 2002**

**Friday, July 12, 2002  
Los Angeles & Palo Alto**

A regular meeting of the Corporations Committee (the "Committee") of the Business Law Section of the State Bar of California was held by video conference at the offices of Milbank, Tweed, Hadley & McCloy in Los Angeles and Mayer, Brown, Rowe & Maw in Palo Alto. Attendance was as follows:

#### **MEMBERS PRESENT:**

Keith Paul Bishop  
David S. Caplan  
John C. Carpenter  
Bruce Dravis  
James K. Dyer, Jr  
Teri Shugart Erickson  
Timothy J. Fitzpatrick  
James F. Fotenos  
Steven K. Hazen

Mark T. Hiraide  
Carol K. Lucas  
Brian D. McAllister  
B. Keith Martin  
David M. Pike  
James R. Walther  
Daniel Weiser  
Neil J Wertlieb  
Nancy Wojtas

#### **MEMBERS ABSENT:**

Nelson D. Crandall  
Eileen Lyon  
Ethna M. Piazza  
Cynthia Ribas  
Randall B. Schai

#### **LIAISONS PRESENT:**

Bradbury R. Clark, Non-Profits Committee  
Suzanne S. Graeser, Executive Committee  
Gail Oshima, Department of Corporations

#### **GUESTS PRESENT:**

Ann Y. Walker, Co-Chair of State Bar Sections (for a portion of the meeting)

The minutes summarize discussions primarily in the order items were listed on the Agenda for the meeting previously circulated to members of the Committee, which is not necessarily the order in which the items were actually taken up at the meeting. The Committee did not take up those topics listed on the Agenda, which are not described in these Minutes.

#### **I. ADMINISTRATIVE MATTERS.**

**A. Opening Remarks and Announcements.** The meeting was brought to order by Co-Chair Neil Wertlieb at approximately 9:30 a.m. Mr. Wertlieb asked members and guests to introduce themselves. Mr. Wertlieb then noted that the next scheduled meeting of the Committee is on August 2nd in San Francisco and the September 6th meeting will be held in Los Angeles. He noted that the regional director of the Securities and Exchange Commission will attend the September 6th meeting of the Committee in Los Angeles. Mr. Wertlieb also noted that the last meeting for this session of the Committee will be held in Monterey on October 11th in conjunction with the State Bar Annual Meeting. Finally, Mr. Wertlieb reported that copies of a comment letter regarding proposed changes to Form 8-K and the FASB exposure draft regarding consolidation of special purpose entities were not included with the meeting materials but are available on request from him.

**B. Approval of Minutes of May 17, 2002 Meeting.** The draft minutes of the meeting of the Committee held on May 17, 2002 and previously circulated to the members of the Committee were approved with minor comments.

## **II. LIAISONS' REPORTS AND DISCUSSION.**

**A. Department of Corporations.** Gail Oshima introduced herself as the new liaison from the Department of Corporations. Ms. Oshima reported that she splits her duties between the Office of Law and Legislation and the Securities Regulation Division of the Department.

**B. BLS Executive Committee.** Suzanne Graeser reported that the State Bar Annual Meeting will be held October 10-13 in Monterey and that the Spring Meeting of the Business Law Section will be held April 3-6, 2003 in conjunction with the ABA annual meeting. Ms. Graeser also noted that the Executive Committee approved the fax filing proposal, subject to certain suggested changes, and the finance lenders proposal submitted by the Committee. Finally, Ms. Graeser noted that the Business Law Section has not been receiving many applications to serve on Section committees. Ms. Lucas commented that a direct mailing to Section members regarding committee memberships may produce better results than simply relying on the Section's website.

**C. Partnerships and Limited Liability Companies Committee.** Steven Hazen provided an update on the activities of the Partnerships and LLC Committee. Mr. Hazen noted that the committee met yesterday and spent some time discussing SB399. Mr. Hazen reported that the Franchise Tax Board and the Secretary of State have each expressed some concerns regarding SB399. The Franchise Tax Board apparently would like SB399 to include a provision that requires the converting entity to pay taxes up to the time of conversion at the rate applicable prior to conversion and at a new rate applicable to the converted entity after conversion. Mr. Hazen noted, however, that it is not exactly clear from the materials circulated to the Partnerships and LLC Committee whether those are actually the concerns of the Franchise Tax Board or if there may be other concerns as well. He noted that the members of that committee had also expressed some uncertainty as to the clarity of the Franchise Tax Board's concerns. The Secretary of State is concerned that the filing fee applicable to a conversion (as drafted, the fee would be \$30) is significantly less than the \$250 fee currently paid when an entity converts. The Secretary of State has proposed a specific fee applicable to conversions (potentially in the range of \$150, although that was not yet definite). The Partnerships and LLC Committee concluded that this was most likely an oversight in the drafting of SB399 and is amenable to the Secretary of State's proposed change in the filing fee and is in agreement with the Franchise Tax Board. Mr. Hazen also reported that the Guide to Limited Liability Companies is now done and each member of the Business Law Section will receive a notice from the State Bar asking them to choose between receiving a hard copy of the Guide or a copy on CD-ROM. The Guide will also be available on the Business Law Section's website for members of the Section. Mr. Hazen further reported that the Partnerships and LLC Committee also considered a report on the FASB exposure draft on consolidation of special purpose entities for financial reporting purposes. The deadline for submitting comments to FASB is August 30th and Mr. Hazen noted that Mr. Bishop had circulated copies of the exposure draft to members of this Committee and requested that members feel free to send him any comments they may have on the exposure draft. Mr. Bishop commented that the proposed FASB changes could affect companies in unexpected ways if a company is required to consolidate entities that in the past may have not been consolidated, resulting, for example, in breach of financial covenants that were negotiated before implementation of any FASB rules requiring such consolidation. Mr. Hazen suggested that it might be advisable to review credit agreements with clients to determine if the proposed FASB rules would impact existing credit agreements with such clients. Messrs. Bishop and Hazen agreed to write a brief summary of the FASB exposure draft for the Committee's website.

**D. ADR Committee.** John Carpenter reported that the ADR Committee met yesterday and that the Franchise Committee has requested that the ADR Committee review the alternate dispute resolution provision in the model form of franchise agreement being prepared by the Franchise Committee. Mr. Carpenter also noted that the next meeting of the ADR Committee will be in

October at the State Bar Annual Meeting.

**E. Health Law Committee.** Carol Lucas reported that the Health Law Committee will become a full standing committee of the Business Law Section starting with the next bar year. She also reported that the Health Law Committee held a joint meeting with the Insurance Committee last month at which John Garimendi was a speaker.

**F. Non-Profits Committee.** Bradbury Clark reported on recent activities of the Non-Profits Committee.

### **III. PENDING LEGISLATION/AFFIRMATIVE LEGISLATIVE PROPOSALS.**

**A. Report of Legislative Liaison.** Mr. Fotenos summarized the following legislation of interest to the Committee:

- **AB601 (Leach)**  
At the Governor's office for signature.
- **AB1875 (Nakano and Correa)**  
Passed the Assembly and now with the Senate Appropriations Committee.
- **AB1995 (Correa)**  
Defeated in the Assembly.
- **AB2187 (Lowenthal)**  
Failed to move out of Committee.
- **AB2355**  
Passed the Assembly. Now with the Senate Judiciary Committee.
- **AB2873 (Frammer and Correa)**  
Passed the Assembly and now with the Senate Appropriations Committee.
- **AB2969 (Florez)**  
At the Governor's office for signature.
- **SB399 (Ackerman)**  
With the Senate Judiciary Committee.
- **SB1472 (Romero)**  
At the Governor's office for signature.
- **SB1473 (Machado)**  
Passed the Senate and now with the Assembly Appropriations Committee.
- **SB1814 (Dunn)**  
Passed the Senate and now with the Senate B&P Committee.

Mr. Fotenos also briefed the Committee on proposed legislation at the federal level resulting from the recent corporate and accounting scandals including (i) S2673 sponsored by Senator Sarbanes, regarding duties of accountants, (ii) SEC Order 4-460 (6/27/02) which requires the CEO and CFO of reporting companies with annual revenue of \$1.2 billion or more to personally certify their company's financial statements and (iii) a recent New York Stock Exchange release

regarding corporate governance.

**B. SB399 (corporate conversions).** Mr. Wertlieb referred to Mr. Hazen's previous comments and also noted that the Partnerships Committee and the Insolvency Committee reached a compromise regarding certain language in SB399, which was acceptable to the staff of the Senate Judiciary Committee. However, new issues raised by the Franchise Tax Board and the Secretary of State (described by Mr. Hazen above) must now be resolved. Mr. Wertlieb suggested that the Committee should not oppose the proposed changes requested by the Franchise Tax Board and the Secretary of State and said that the subcommittee delegated authority by the committee to deal with these issues will monitor the bill through the legislative process and handle issues as they arise. Members of the Committee unanimously approved this approach.

**C. Section 25102(o) Regulation Comments.** Mr. Bishop reported that the proposed 25102(o) regulations are still pending with the Department of Corporations.

**D. Section 710 (sunset on supermajority approvals).** Mr. Pike reported that the bill is at the Governor's office for signature.

**E. Technical Corrections Bill.** Mr. Wertlieb reported that the bill is at the Governor's office for signature.

Mr. Wertlieb thanked the members of the Committee for their work on the various legislative proposals that passed the legislature this year. Several members also commented on the commendable job Terry Miller has been doing in assisting members in steering proposals through the legislative process. Members complimented Mr. Miller's responsiveness to issues and his many contacts in Sacramento and expressed their desire that he continue to work with the State Bar.

#### **IV. POTENTIAL AFFIRMATIVE LEGISLATIVE PROPOSALS.**

**A. Secretary of State Fax Filings.** Mr. Dravis reported that the fax filing legislative proposal has been approved by the Executive Committee, with some changes suggested by that committee to clarify that "facsimile signature" refers only to a document with an original signature that is subsequently transmitted by facsimile. Members discussed whether the concept of "facsimile signature" should be expanded to include signatures other than a manual signature (for example, by rubber stamp or other mechanical or electronic means) and concluded that it should be limited to a facsimile of an original signature. Mr. Walther agreed to work with Mr. Dravis to make final changes to the legislative proposal.

**B. 25118(b) Definition of Aggregate Evidence of Indebtedness.** Mr. Weiser led a discussion concerning Section 25118(b) and reported that he had revised a memo summarizing relevant issues which he will distribute to members of the Committee. Mr. Weiser also reported that he spoke with several people who worked on the original amendment to Section 25118(b) as well as members of the UCC Committee to get more background concerning this law. He stated that many states exclude a borrower that is a corporation from usury laws and that exempting corporations from 25118(b) and/or clarifying that the \$300,000 indebtedness limit applies to future drawdowns under a loan facility as well as any modifications of existing indebtedness may be potential amendments worthy of further review. Members voted to authorize Mr. Weiser to prepare a legislative proposal summarizing the above.

**C. Amend Finance Lenders Law.** Mr. Bishop reported that the Executive Committee has approved the legislative proposal creating an exemption for venture capital firms from the licensing provisions of the finance lenders law. Mr. Bishop noted that, after a sponsor is found, this proposal will be submitted to the legislature in 2003.

#### **V. WEB SITE PROJECTS.**



**A. Website Update.** Mr. Caplan requested that members of the Committee responsible for various Committee projects review the Committee website to see if the descriptions of projects are accurate.

**B. Recent Developments.** Ms. Wojtas reported that she will send Mr. Caplan a list of recent developments to be posted on the Committee's website.

## **VI. OTHER PROJECTS.**

**A. Educational Activities.** Mr. Dravis reported that the Committee will present two programs at the State Bar annual meeting in October - fiduciary duties of directors and California law regarding entity formation. Mr. Dravis also reported that Ms. Ribas is using the presentation materials for the program she and Roy Schmidt chaired on comparison of California and Delaware corporate law at the Spring Meeting of the Business Law Section to draft an article for The Business Law News.

**B. Blue Sky Guide.** Mr. Bishop reported that the Blue Sky Guide is close to completion.

**C. 25102(f) Regulations/Legislative Proposal.** Mr. Fitzpatrick reported that this proposal has been deferred until the 2003 legislation session.

**D. California Law re: Director Duties to Creditors.** Mr. Weiser led a discussion concerning directors' fiduciary duties owed to creditors of an insolvent corporation. Mr. Weiser summarized the In re Jacks approach which states that a director's duties to creditors are limited to those set forth in the Corporations Code. He also discussed a "safe harbor" approach which would protect directors attempting to balance competing interests in an insolvent corporation. Members voted to authorize Mr. Weiser to prepare an initial draft of a legislative proposal incorporating the safe harbor approach.

## **VII. NEW BUSINESS**

**A, Practice Issues.** Ann Walker led a discussion of issues arising in connection with "pay to play" provisions in the articles of incorporation of a California corporation.

The meeting was adjourned at approximately 12:30 p.m.

/s/ David M. Pike  
David M. Pike  
Secretary

**Corporation Committee Meeting Minutes**

